Supreme Court, U.S.
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No. 95107 8 JAN 3 - 1996

In The OFFICE OF THE CLERK

Supreme Court of the United States

October Term, 1995

JAMES H. CONNETT,

Petitioner,

vs.

JUSTUS ENTERPRISES OF KANSAS, INC., aka Justus Cylinder-Technology, Inc.; JUSTUS CYLINDER-TECHNOLOGY, INC.; RANSON & COMPANY, INC.; MID CONTINENT MUNICIPAL INVESTMENTS, INC.; J.O. DAVIDSON & ASSOCIATES, INC.; R.G. DICKINSON & CO.,

Respondents.

Petition for Writ of Certiorari to the United States Court of Appeals for the Tenth Circuit

PETITION FOR WRIT OF CERTIORARI

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QUESTION PRESENTED

Whether the United States District Court and the United States Court of Appeals for the Tenth Circuit erred, by weighing conflicting evidence, determining witness credibility, and generally invading the province of the jury, in ruling that Defendants were entitled to judgment as a matter of law pursuant to Fed. R. Civ. P. 50.

PARTIES TO THE PROCEEDING

Plaintiff/Appellant/Petitioner:

James H. Connett

Defendants/Appellees/Respondents:

Ranson & Company, Inc.;
Mid-Continent Municipal Investments, Inc.;
J.O. Davidson & Associates, Inc.; and
R.G. Dickinson & Company (now Dickinson & Company)

TABLE OF CONTENTS

	Page
Question Presented	i
Parties to the Proceeding	ii
Table of Contents	iii
Table of Citations	iii
Opinions Below	1
Statement of Jurisdiction	1
Statutory Provisions Involved	1
Statement of the Case	2
Reasons for Granting the Writ	7
I. The appeals court decision has sanctioned a departure by the District Court from the accepted and usual course of judicial proceedings.	8
Conclusion	17

TABLE OF CITATIONS

Cases Cited:

Boodoo v. Cary, 21 F.3d 1157 (D.C. Cir. 1994)	11
Garcia v. Cordova, 930 F.2d 826 (10th Cir. 1991)	9

Contents

Page

Lytle v. Household Manufacturing, 494 U.S. 545, 108 L. Ed. 2d 504, 110 S. Ct. 1331 (1990) 10

Motive Parts Warehouse v. Facet Enterprises, 774 F.2d 380 (10th Cir. 1985) 10, 16

TSC Industries v. Northway, Inc., 426 U.S. 438, 48 L. Ed. 2d 757, 96 S. Ct. 2126 (1976) 9

Walker v. Action Industries, Inc., 802 F.2d 703 (4th Cir. 1986), *cert. denied*, 479 U.S. 1065, 93 L. Ed. 2d 1000, 107 S. Ct. 952, *reh. denied*, 480 U.S. 926, 94 L. Ed. 2d 703, 107 S. Ct. 1389 (1987) 15

Statutes Cited:

15 U.S.C. § 78j 1

28 U.S.C. § 1254(1) 1

28 U.S.C. § 1331 ..... 1, 2

United States Constitution:

Seventh Amendment 1, 11, 17

Rules Cited:

Federal Rule of Civil Procedure 50 ..... i, 1, 7

Federal Rule of Civil Procedure 50(a) 2

Contents

	Page
Federal Rule of Civil Procedure 50(a)(1)	8
Supreme Court Rule 10(a)	8
Other Authorities Cited:	
17 C.F.R. § 230.175	15
17 C.F.R. § 240.10b-5	8
APPENDIX	
Appendix A — Opinion of the United States Court of Appeals for the Tenth Circuit Filed October 5, 1995 ...	1a
Appendix B — Memorandum and Order of the United States District Court for the District of Kansas Filed July 21, 1994	14a
Appendix C — Memorandum and Order of the United States District Court for the District of Kansas Filed May 4, 1994	25a
Appendix D — Rule, Constitutional Provision and Statute Involved	45a

The Petitioner, James H. Connett, respectfully prays that a Writ of Certiorari be issued to review the judgment and opinion of the United States Court of Appeals for the Tenth Circuit issued in the above proceeding on October 5, 1995.

OPINIONS BELOW

The opinion of the Court of Appeals (App. A), of which review is sought, is reported at 68 F.3d 382 (10th Cir. 1995). That opinion held that the judgment of the United States District Court for the District of Kansas (App. C) should be affirmed wherein Defendants were granted a judgment as a matter of law, pursuant to Fed. R. Civ. P. 50. The District Court order is not reported. The District Court also issued a decision on July 22, 1994, wherein it denied Petitioner's motions to alter or amend judgment or for new trial. (App. B).

STATEMENT OF JURISDICTION

The opinion of the Court of Appeals was entered on October 5, 1995. (App. A). This Court's jurisdiction is invoked under 28 U.S.C. § 1254(1). Jurisdiction in the District Court was invoked under 28 U.S.C. § 1331, which establishes original jurisdiction in the federal District Court of all civil actions arising under federal law.

STATUTORY PROVISIONS INVOLVED

This case involves the relationship between Fed. R. Civ. P. 50 and § 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j, as well as the Seventh Amendment to the United States Constitution. (App. D).

STATEMENT OF THE CASE

A Writ of Certiorari is requested in this case to allow this Court to review the Court of Appeals opinion (App. A), which affirmed the District Court's order entering judgment as a matter of law in favor of the Defendants. (App. C). A brief summary of the background facts and the proceedings is as follows.

The Petitioner represents a class that brought this action for damages for securities fraud and common law fraud against the lessee, the underwriters, and their agents with respect to an industrial revenue bond issue. Jurisdiction in the federal District Court was invoked under 28 U.S.C. § 1331, which establishes original jurisdiction in the federal District Court of all civil actions arising under federal law. After disposition of claims against all parties, except four of the underwriters, which are parties to this Writ, trial commenced to a jury. At the conclusion of Petitioner's evidence, the trial court sustained the Defendants' motion for judgment as a matter of law pursuant to Fed. R. Civ. P. 50(a). (App. C). The Petitioner moved for a rehearing and for new trial, which were denied by the trial court. (App. B). The Tenth Circuit affirmed the District Court's order of judgment as a matter of law on Petitioner's appeal. (App. A).

The case arises from the Petitioner's purchase of industrial development revenue bonds. In the Fall of 1983, the City of Chanute, Kansas, issued $6.6 million dollars in industrial development revenue bonds. The tenant industry for whom the bonds were issued was Justus Enterprises of Kansas, Inc. Personal guarantor of the bonds was Walter Justus of Indianapolis, Indiana. The bonds were purchased for resale to the public by an underwriting syndicate consisting of Ranson & Company, Inc., R.G. Dickinson & Company, B.C.

Christopher Securities Company, J.O. Davidson & Associates, Inc., and Mid-Continent Municipal Investments, Inc. The syndicate was headed by Ranson acting through its vice-president, Carlos Taylor. Counsel for the underwriters was the firm of Fleeson, Gooing, Coulson & Kitch of Wichita, Kansas. The proceeds from the sale of the bonds were used to buy the physical assets of Cylinder Technologies, Inc., which were used by that company to manufacture seamless metal cylinders in Chanute, Kansas.

The form of public offering was by way of an official statement dated October 31, 1983. Among the purchasers of the original issue were Petitioner and Gordon Henke, another member of the class, who both testified at trial. The offer and sale of the bonds were accomplished through the use of the mails and instrumentalities of interstate commerce.

Justus Enterprises of Kansas, Inc., as tenant, defaulted under the terms of the lease with the City of Chanute when it failed to pay the rent due under the lease for January, 1986 and thereafter. On January 27, 1986, Southwest National Bank, as Trustee of the City of Chanute, Kansas, notified Walter G. Justus, guarantor, and Defendant Justus Enterprises of Kansas, Inc., of the default and gave them thirty (30) days written notice to cure the default. The guarantors failed to cure and had defaulted under the terms of their guarantees.

On February 27, 1986, Walter G. Justus filed proceedings in the United States Bankruptcy Court, District of Indiana, Case No. IP86-01163-V. Southwest National Bank, as Trustee, learned of the Walter G. Justus bankruptcy at approximately March 1, 1986, and on March 3, 1986, Southwest National Bank, as Trustee, notified Petitioner and members of Petitioner's class of the defaults under the bond documents.

After the default, the sum of $388,394.22 was realized from the sale of the property, plant and equipment purchased with the bond proceeds.

This action was filed on December 31, 1987. Among Petitioner's many contentions at the District Court level, was the claim that the bond purchasers were misled to believe that the property to be purchased with the bond proceeds had a value greatly in excess of the $388,394.22, which was realized from the sale of the assets. In fact, Petitioner was led to believe that the value was significantly in excess of the total of the bond issue.

The official statement upon which Petitioner relied states that the $3,924,000 of the bond proceeds were to be applied to the purchase of the facilities from Cylinder Technologies, Inc., and contains the following statement:

> Bond proceeds will be used to acquire approximately 5 acres of land, 2 connected multipurpose buildings totaling 77,000 square feet, and machinery and equipment owned by Cylinder Technology, Inc., "(CTI)" in Chanute, Kansas. **The total appraised value of the acquired assets, including those not acquired out of bond proceeds, as determined by its "fair market value in continued use" based on an appraisal, as of May 31, 1982, by a nationally known independent appraisal company, was in excess of $11 million dollars.**

Emphasis added. (App A, 4a).

The official statement also states:

> In the opinion of management, **Justus Enterprises has acquired a substantial unrecorded equity due to the favorable negotiated purchase price** of $3,925,000.00 for the acquisition of assets from CTI.

Emphasis added. (*See*, App. A, 8a).

Respondents were aware that, at the time when the appraisal company had appraised the assets, the appraisers valued the assets in two different ways. First was continued use of the assets, as was set forth in the Official Statement. Second was liquidation in an orderly manner value. Respondents, however, did not disclose the appraised liquidation value of approximately $1.5 million. (App. A, 3a-4a).

Furthermore, the evidence showed that Respondents were aware of the competing appraisals and made a conscious, intentional decision to include the $11,000,000 appraisal and eliminate the $1.5 million appraisal. (App. A, 4a). Michael Shotts, an employee of Walter Justus, testified that he conversed with Carlos Taylor of Ranson, regarding the orderly liquidation value appraisal and stated that, "it was obvious that the amount of that appraisal would not suffice for what it was needed for" and "it was decided that it would be best to go back to the same apprais[er] since they had done one and get an update based on the going concern." (Tr. 216-17; R. App. 134-35).

Also, the appraisal company notified Respondents of certain assumptions upon which it relied in its "fair market

value in continued use" valuation of the assets of over $11,000,000. Likewise, these assumptions were not included in the Official Statement. The appraisal company stated that the following conditions and limitations applied to the "continued use" appraisal:

> "Fair market value" is defined as the estimated amount at which the property might be expected to exchange between a willing buyer and a willing seller, neither being under compulsion, each having reasonable knowledge of all relevant facts, with equity to both, and with buyer and seller contemplating the retention of the facilities at their present location for the continuation of the current operations.
>
> * * *
>
> We did not investigate any financial data pertaining to the present or perspective earning capacity of the operation in which the designated property is used. Our opinion of fair market value assumes that the prospective earnings will provide a fair return upon the appraised value of the assets included in the appraisal, as well as assets not part of the appraisal, if any, and adequate net working capital.
>
> * * *
>
> The appraised fair market value stated above is not intended to represent the amount that might be realized from

> disposition of the property in the open market for any alternate applicable use.

(App. A, 10a-11a).

Contrary to allegations that Petitioner could have obtained further, relevant appraisal information by inquiring of the Respondents (App. A, 11a, fn. 5), the evidence presented indicates that the appraisal company only permitted the Respondents to reference the appraisal in the manner indicated in the Official Statement. The appraiser's permission to use this language was based upon the understanding that this would be the only reference in the Official Statement to the appraisal . (App. B, 17a-18a). There was no evidence that the appraisal company ever authorized disclosure of any other information to any prospective bond purchasers.

The bond purchasers testified that they relied upon the Official Statement in their purchase of the bonds. (Tr. 33, 572; R. App. 131, 153). Each testified that if he had been advised of the information set forth above concerning the liquidation value appraisal and the assumptions underlying the "fair market value in continued use" appraisal, he would not have bought the bonds. (Tr. 45, 211, 572-76; R. App. 132, 133, 153-57).

There were other material facts presented to the District Court, but, on appeal, Petitioner relies only upon the foregoing statements of fact in asserting that Defendants was not entitled to judgment as a matter of law pursuant to Fed. R. Civ. P. 50.

REASONS FOR GRANTING THE WRIT

The decision of the Court of Appeals in this case departs from the accepted and usual course of judicial proceedings and

has also sanctioned such departure by the lower court, so as to call for the exercise of the Supreme Court's power of supervision. Supreme Court Rule 10(a).

I.

THE APPEALS COURT DECISION HAS SANCTIONED A DEPARTURE BY THE DISTRICT COURT FROM THE ACCEPTED AND USUAL COURSE OF JUDICIAL PROCEEDINGS.

The Court of Appeals decision, affirming the District Court's judgment as a matter of law in favor of Respondents, departs from the accepted and usual course of judicial proceedings in that it is not the duty of the trial court judge, or the Court of Appeals to invade the province of the jury and decide factual issues. Rule 50(a)(1) provides:

> If, during a trial by jury, a party has been fully heard on an issue and there is no legally sufficient evidentiary basis for a reasonable jury to find for that party on that issue, the court may determine the issue against a party and may grant a motion for judgment as a matter of law against that party with respect to a claim or defense that cannot under the controlling law, be maintained or defeated without a favorable finding on that issue.

As this Court is well aware, Rule 10b-5 (17 C.F.R. § 240.10b-5) provides that:

> It shall be unlawful for any person, directly or indirectly, by use of any means or

> instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,
>
> * * *
>
> (b) to make any untrue statement of a material fact or to **omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they are made, not misleading,** . . . in connection with the purchase or sale of any security. [Emphasis added.]

The Court of Appeals correctly found that the issue of materiality was important in determining whether to affirm the District Court's ruling in favor of Respondents' Motion for Judgment as a matter of law. (App. A, 6a-7a). It is true that liability for failure to disclose only arises when a duty to disclose exists and the withheld information is material. The Court of Appeals, however, incorrectly held that it could rule on the question of materiality as a matter of law.

The Tenth Circuit recognized that, generally, materiality is more a factual question under a mixed standard of review than a legal question, and it may only be resolved as a matter of law when the information is "so obviously important (or unimportant) to an investor, that reasonable minds cannot differ on the question of materiality." (App. A, 5a; citing *Garcia v. Cordova*, 930 F.2d 826, 829 (10th Cir. 1991), quoting *TSC Industries v. Northway, Inc.*, 426 U.S. 438, 48 L. Ed. 2d 757, 96 S. Ct. 2126 (1976)). However, when the Court of Appeals affirmed the District Court's decision, it failed to apply the proper standard of review, which would have caused the appellate court to overrule the District Court's ruling.

When ruling on a motion for judgment as a matter of law, the trial court and the appellate court must not weigh the evidence, but draw all factual inferences in favor of the non-moving party. *Lytle v. Household Manufacturing*, 494 U.S. 545, 554, 108 L. Ed. 2d 504, 110 S. Ct. 1331 (1990). In other words:

> The trial court may direct a verdict only where the evidence and all inferences to be drawn therefrom are so clear that reasonable minds could not differ on the conclusion. [Citations omitted.] The evidence must be viewed in the light most favorable to the party against the whom the directed verdict is sought, and if, on the basis on the evidence and inferences to be drawn therefrom, reasonable and fair minded persons might form different conclusions as to the facts in issue, a directed verdict is improper. [Citations omitted.] Stated another way, a directed verdict is justified only if the proof is all one way or so overwhelmingly preponderant in favor of the movant as to permit no other rational conclusion. [Citations omitted.]

Motive Parts Warehouse v. Facet Enterprises, 774 F.2d 380, 385-86 (10th Cir. 1985).

In the case at bar, the Court of Appeals failed to use this standard, and weighed the evidence to determine that: (a) the omission of the "orderly liquidation value" appraisal did not render the official statement misleading; and (b) omitting assumptions underlying the "fair market value and continued

use" appraisal did not render misleading the appraisal information actually disclosed. (App. A, 10a, 13a).

A judgment as a matter of law is highly disfavored by the courts because decisions on factual matters should be left to the jury. *Boodoo v. Cary*, 21 F.3d 1157, 1161 (D.C. Cir. 1994). An analysis of the rulings of both courts shows that the courts weighed the evidence, determined witness credibility, and in other ways "intrude[d] upon the rightful province of the jury." *Id.*

The Tenth Circuit opinion indicates that the court did weigh the evidence when it made its decision. Specifically, Section III of the opinion is nothing more than the appellate court's opinion as to what a jury would conclude from the evidence presented. (App. A, 8a-13a). The trial court did the same. There are numerous comments in the trial court decisions indicating the court's views of witness credibility and its weighing of the evidence. (App. A, App. B). By doing so, the courts deprived Petitioner of his right to a trial by jury in civil cases as guaranteed by the Seventh Amendment to the United States Constitution. The Seventh Amendment provides:

> In Suits, a common law, where the value in controversy shall exceed twenty dollars, the right of trial by jury shall be preserved, and no fact tried by a jury shall be otherwise re-examined in any Court of the United States, then according to the rules of common law.

United States Constitution, Amendment VII.

For example, in the Tenth Circuit opinion, the court states:

> Plaintiff asserts that the omission of the "orderly liquidation value" appraisal from the Official Statement misleads investors to conclude that the assets purchased with bond proceeds are sufficiently valuable to avoid a loss.

(App. A, 8a). This statement misinterprets Petitioner's claim. The affirmative representation of the $11,000,000 appraisal, plus the "unrecorded equity" statement, both found in the Official Statement, are rendered misleading by the absence of the $1.5 million liquidation value appraisal. Petitioner's allegation turns out to be true based upon the evidence presented at trial. Instead of weighing these facts and the inferences that can be drawn therefrom in favor of Petitioner, the Tenth Circuit argued facts that supported Respondents' position and construed the evidence in Respondents' favor, including generic *caveats* included in all solicitation material. (App. A, 9a).

The court's conclusions that a reasonable investor would not find the omissions material conflicts with the evidence presented. Petitioner and another investor each testified that they relied upon the Official Statement in their purchase of the bonds. (Tr. 33, 572; R. App. 131, 153). Furthermore, each testified that if he had been advised of the information set forth above concerning the liquidation value appraisal and the assumptions underlying the "fair market value in continued use" appraisal, he would not have bought the bonds. (Tr. 45, 211, 572-76; R. App. 132, 133, 153-57). The fact that the court weighed the evidence presented in favor, not of Petitioner, but in favor of Respondents can be seen in the following language quoted from the opinion:

> Plaintiff points to the district court's

> statement that the "orderly liquidation value" would likely be important information to a reasonable investor as demonstrating the district court applied the wrong legal standard. Read in isolation, this might appear to be so. A reading of the entire opinion, however, reveals that the district court considered all of plaintiff's evidence and discussed specific disclosures that communicated risks to bond purchasers, including that CTI was a "troubled financial condition." *Id.* at 56. We agree with the district court that the omission of the "orderly liquidation value" appraisal did not render the Official Statement misleading.

(App. A, 9a-10a).

Clearly, the language utilized indicates that the court lightly considered the evidence in Petitioner's favor (*i.e.*, omission of $1.5 million appraisal) while placing great weight on that in favor of Respondents (*i.e.*, general disclosures that the value of the assets may not be as great as that indicated in the appraisal). The facts should be construed in Petitioner's favor. Respondents included specific appraisal information that would induce investors to purchase the bonds. It did not include specific appraisal information that would clarify the usefulness of the $11,000,000 appraisal (*i.e.*, the $1.5 million appraisal). In fact, the record indicates that Respondents considered the liquidation value appraisal so dismal that "it was obvious that the amount of that appraisal would not suffice for what it was needed for" and "it was decided that it would be best to go back to the same apprais[er] since they had done one and get an update based on the going concern" (Tr.

216-16). Instead of construing these facts in Petitioner's favor the court opted to weigh the evidence in favor of Respondents to rule that no reasonable investor could find the omitted information material.

With regard to the omission of the assumptions underlying the $11,000,000 appraisal, it is, likewise, clear that the court did not construe the facts presented in favor of Petitioner, but weighed the conflicting evidence in favor of Respondents. Respondents again, included specific information that would aid in the sale of the bonds, but included vague admonitions warning investors that they should not put much faith in the information actually disclosed.

Not only did Respondents state that the assets acquired were valued at over $11,000,000 but they indicated an "unrecorded equity" would be realized when the bond proceeds of nearly $3.5 million were used to purchase these assets. (App. A, 8a). The assumptions underlying the appraisal, however, clearly indicate that the numbers included in the Official Statement were *pie in the sky* numbers not based upon the "prospective earning capacity of the operation," but on the assumption that the value of the assets appraised "will provide an [sic] fair return. . . ." (App. A, 10a-11a). Similarly the assumptions state that the "appraised fair market value stated above is not intended to represent the amount that might be realized from disposition of the property in the open market. . . ." *Id.* It is obvious, when the evidence is properly construed in Petitioner's favor, that this omitted information would be material to an investor who was just told these assets were worth over $11,000,000. The court stated that a reasonable investor would conclude the "in continued use" appraisal assumes a viable business operation and does not include a sale of those business assets for another purpose. (App. A, 11a). This overlooks the fact that the appraisal did not

even consider whether there was a viable business operation to evaluate. Again, the court improperly construed the evidence presented in favor of the movant, not in favor of the Petitioner.

The extent to which the Court of Appeals violated Petitioner's right to a jury trial can be seen from an examination of the type of information that the court determined was not misleading. The opinion indicates that inclusion of the appraisal value of the "fair market value in continued use" was not misleading even when the "orderly liquidation value" appraisal or the assumptions that underlied the "fair market value continued use" appraisal were omitted. (App. A, 10a, 13a). The use of "soft information" (*e.g.*, asset appraisals and future earnings predictions) is seen as inherently misleading. In fact, the Securities Exchange Commission (SEC) had a policy of preventing the use of "soft information" in disclosure documents on the basis that such information is likely to mislead investors. *Walker v. Action Industries, Inc.*, 802 F.2d 703, 707 (4th Cir. 1986), *cert. denied*, 479 U.S. 1065, 93 L. Ed. 2d 1000, 107 S. Ct. 952, *reh. denied*, 480 U.S. 926, 94 L. Ed. 2d 703, 107 S. Ct. 1389 (1987). The *Walker* case indicates, however, that the SEC began to allow "soft information" to be included in disclosures if they are made in "good faith." *Id.* at 707; *see* 17 C.F.R. § 230.175 (1985). The fact that such information is likely to mislead investors, however, is still adhered to in the courts. The Fourth Circuit still recognizes that the use of "soft information" does lead to uncertainty and is likely to mislead investors. *Walker*, 802 F.2d at 709. Therefore, the fact that this type of information has been deemed by the SEC and by the courts to be potentially misleading is a factor that weighs in favor of Petitioner in consideration of Respondents' motion for judgment as a matter of law. The appellate court opinion, however, did not recognize this fact and, as such, did not weigh all inferences in Petitioner's favor when ruling on Respondents' motion.

Furthermore, by actually comparing the evidence, the appellate court implicitly recognizes that there is proof in favor of Petitioner. As a result, there is no possible way that "the proof is all one way or so overwhelmingly preponderant in favor of the movant as to permit no other rational conclusion." *Motive Parts*, 774 F.2d at 386. The logical inferences derived from the evidence make it clear that Respondents intentionally included specific information concerning the appraisals in the Official Statement to induce investors to purchase the bonds, while deleting specific references to such information that would put investors on notice of the lack of reliability of representations made. Consequently, the representations concerning the $11,000,000 appraisal of the assets were rendered misleading by the omission of the specific information that fully explained this value. The defect of omitting this specific information cannot be cured by offering vague warnings to investors.

It is clear from the foregoing that the appellate court, in order to reach the conclusion it did, weighed the evidence and determined its credibility. It resolved fact issues in favor of Respondents. When evidence presented is not so one way or so overwhelmingly preponderant in favor of Respondents as to permit no other rational conclusion, and all the inferences that can be drawn from this evidence are weighed in Petitioner's favor, it is clear that the lower courts erred in ruling that a reasonable investor could not find the omitted information to be material. This determination is meant to be left to a jury in cases such as these. The standard of review the courts should have used in ruling on Respondents' motion for judgment as a matter of law was violated. As such, Petitioner's constitutional right to a trial by jury was also violated.

CONCLUSION

The Tenth Circuit erred in ruling in favor of Respondents on their motion for judgment as a matter of law. The standard of review to be followed requires that the evidence must be viewed in the light most favorable to the Petitioner. When this is done in the present case, it is **NOT** clear that reasonable minds could not come to different conclusions based upon the evidence presented by the Petitioner. Furthermore, the evidence presented by Petitioner was **NOT** all one way or so overwhelmingly preponderant in favor of movant as to permit no other rational conclusion. In so erring, the Court of Appeals denied Petitioner his Seventh Amendment right to a trial by jury. Furthermore, by invading the province of the jury, weighing the evidence, and applying an incorrect standard in ruling on Respondents' motion for judgment as a matter of law, the Court of Appeals has so far departed from the accepted and the usual course of judicial proceedings, that it requires the Supreme Court to exercise its power of supervision. Therefore, the Writ of Certiorari should be granted.

Respectfully submitted,

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APPENDIX A — OPINION OF THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT FILED OCTOBER 5, 1995

PUBLISH

UNITED STATES COURT OF APPEALS
TENTH CIRCUIT

No. 94-3298

JAMES H. CONNETT,

Plaintiff-Appellant,

v.

JUSTUS ENTERPRISES OF KANSAS, INC., aka Justus Cylinder-Technology, Inc.; JUSTUS CYLINDER-TECHNOLOGY, INC.; RANSON & COMPANY, INC.; MID CONTINENT MUNICIPAL INVESTMENTS, INC.; B.C. CHRISTOPHER SECURITIES CO.; J.O. DAVIDSON & ASSOCIATES, INC.; R.G. DICKINSON & CO.; CARLOS TAYLOR,

Defendants-Appellees.

Appeal from the United States District Court
for the District of Kansas
(D.C. No. 89-CV-1739)

Submitted on the briefs:

Frank C. McMaster of McMaster & McMaster, and Thomas A. Wood, Wichita, Kansas, for Plaintiff-Appellant.

Appendix A

Robert J. O'Connor and David E. Bengston of Morrison & Hecker, Wichita, Kansas, for Defendants-Appellees.

Before HENRY and LOGAN, Circuit Judges, and ELLISON, District Judge.*

LOGAN, Circuit Judge.

Plaintiff James H. Connett appeals from a district court judgment entered in favor of defendants Ranson and Co., Inc., Mid-Continent Municipal Investments, Inc., J.O. Davidson & Assoc., Inc. and R.G. Dickinson & Co. (collectively defendants or the bond sellers). The suit alleged violation of § 10(b) of the Securities and Exchange Act of 1934, 15 U.S.C. § 78j, as well as common law fraud under Kansas law in connection with the sale of industrial revenue bonds issued by the City of Chanute, Kansas. On appeal plaintiff asserts that the district court erred in granting defendants' motion for judgment as a matter of law at the close of plaintiff's evidence. Plaintiff contends that he presented a legally sufficient case to require submission to the jury of the issue whether the Official Statement prepared in connection with the bond offering omitted material information rendering it misleading under Rule 10b-5.[1]

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* The Honorable James O. Ellison, Senior United States District Judge, United States District Court for the Northern District of Oklahoma, sitting by designation.

1. After examining the briefs and appellate record, this panel has determined unanimously that oral argument would not materially assist the determination of this appeal. *See* Fed. R. App. P. 34(a); 10th Cir. R. 34.1.9. The case is therefore ordered submitted without oral argument.

Appendix A

I

Justus Enterprises of Kansas, Inc. was incorporated specifically to acquire the assets of Cylinder Technology, Inc. (CTI) and to operate its business. The purchase price for the five acres of land, two buildings, machinery and equipment of CTI, a manufacturer of high-pressure cylinders, was $3,924,000. The City of Chanute issued $6.6 million of industrial revenue bonds to fund the acquisition, to purchase additional machinery and building improvements, to create a bond reserve and an escrow of the first six months interest, and to pay the bond issuance expense. The city took title and leased the assets to Justus Enterprises pursuant to a typical industrial revenue bond lease-purchase agreement. The security for the payment of the bonds was the lease, the acquired assets, and the personal guarantees of Justus Enterprises and Walter G. Justus.

Justus Enterprises defaulted on the bonds and Walter Justus filed for bankruptcy. When a liquidation sale of the company properties brought in less than $400,000, plaintiff filed suit individually and as a class representative for the bond purchasers (excluding the defendants). The district court certified plaintiff as class representative for purchasers in the initial bond offering.[2] Plaintiff alleged, inter alia, that the bond sellers committed fraud by failing to disclose certain appraisal information.[3]

The omitted information appears in various appraisal documents generated by American Appraisers (American). In

2. Before trial, all defendants except the bond sellers who are a party to this appeal were either dismissed or settled their claims. *See* App. 59.

3. Plaintiff evidently concedes that his claim is based only upon omissions in the Official Statement; he does not challenge the accuracy of the information that was disclosed to potential investors.

Appendix A

1982, American made a fair market value appraisal of the assets of C.J.B. Industries, Inc., in Chanute, Kansas, for CTI when CTI purchased those assets. In August 1983 American made a $1.5 million "orderly liquidation value" appraisal of the assets at CTI's request. American also provided CTI with a fair market value appraisal in September 1983. Correspondence followed between American, bond counsel, and Ranson regarding what information from American's appraisals would be included in documents generated in connection with the industrial revenue bond issue. The Official Statement that plaintiff argues is misleading was dated October 31, 1983.

The Official Statement contained a "Description of Project" reading as follows:

> Bond proceeds will be used to acquire approximately five acres of land, two connected multi-purpose buildings totaling 77,000 square feet, and machinery and equipment owned by Cylinder Technology, Inc. ("CTI") in Chanute, Kansas. The total appraised value of the acquired assets, including those not acquired out of bond proceeds, as determined by its "fair market value in continued use" based on an appraisal, as of May 31, 1982, by a nationally known independent appraisal company, was in excess of $11,000,000. The Tenant [Justus Enterprises] is expected to pay approximately $180,000 for additional assets of CTI and new machery [sic] and equipment, and to pay $105,000 for organizational and acquisitional expenses from Tenant's own funds.

App. 93. The omitted information falls into two categories. One was the "orderly liquidation value" of the assets from American's August 1983 appraisal letter. *See id.* at 75-77. The other category includes the underlying assumptions for the "in continued use" appraisal from American's September 1983 appraisal letter. *See id.* at 81-83. The only appraisal figure included in the Official Statement was the single agreed-upon reference to the "fair market value in continued use." *Id.* at 84, 93; Supp. App. 84.

At the close of plaintiff's evidence during a jury trial, the district court granted the bond sellers' Fed. R. Civ. P. 50(a) motion for judgment as a matter of law. The district court found that plaintiff made "no showing that the [bond sellers] knowingly made false or misleading representations or omissions of material facts in connection with the sale of the bonds." App. 58.

We review a district court order disposing of a Rule 50 motion de novo, construing the evidence and making reasonable inferences most favorable to the nonmoving party. *Pegasus Helicopters, Inc. v. United Technologies Corp.*, 35 F.3d 507, 510 (10th Cir. 1994). Our analysis necessarily examines the materiality of the omitted information. Materiality is a mixed question of law and fact. *TSC Indus., Inc. v. Northway, Inc.*, 426 U.S. at 450 (1976). "Although generally more a factual question under the mixed standard of review, the question of materiality is to be resolved as a matter of law when the information is 'so obviously important [or unimportant] to an investor, that reasonable minds cannot differ on the question of materiality.' " *Garcia v. Cordova*, 930 F.2d 826, 829 (10th Cir. 1991) (quoting *TSC Indus., Inc.*, 426 U.S. at 444 (citations omitted)).

Appendix A

II

We first address the legal standard for a material nondisclosure under § 10(b)-5[4] and Rule 10b-5 promulgated under that statute. Rule 10b-5 provides in pertinent part that

> It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,
>
> . . .
>
> (b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements

4. That section, 15 U.S.C. § 78j, reads as follows:

> Manipulative and deceptive devices
>
> It shall be unlawful for any person, directly or indirectly, by the use of any means of instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange —
>
> . . .
>
> (b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

> made, in the light of the circumstances under which they were made, not misleading, . . . in connection with the purchase or sale of any security.

17 C.F.R. § 240.10b-5.

Liability for failure to disclose only arises when the duty to disclose exists and the withheld information is material. *Affiliated Ute Citizens v. United States*, 406 U.S. 128, 152-54; *see also Chiarella v. United States*, 445 U.S. 222, 227-29 (1980); *Jensen v. Kimble*, 1 F.3d 1073, 1077 (10th Cir. 1993) (in order to be actionable, an omission must render *misleading* the affirmative statements actually made). Although the Supreme Court has defined materiality in terms of importance to investors, it has also explained that "there must be a substantial likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the 'total mix' of information made available." *TSC Indus., Inc. v. Northway, Inc.*, 426 U.S. 438, 449 (1976); *see also Basic Inc. v. Levinson*, 485 U.S. 224, 238 (1988) (expressly adopting the *TSC Industries* standard of materiality for § 10(b) and Rule 10b-5). Thus we must evaluate the omissions in light of all the information included in the Official Statement, to determine if it would have affected that mix. 426 U.S. at 449; *see also Garcia v. Cordova*, 930 F.2d 826, 829 (10th Cir. 1991).

Appendix A

III

A

Plaintiff asserts that the omission of the "orderly liquidation value" appraisal from the Official Statement misleads investors to conclude that the assets purchased with bond proceeds are sufficiently valuable to avoid a loss. This argument ignores the evidence in the record.

The appraisal value of over $11,000,000 in the Official Statement is qualified as being the "fair market value in continued use" and is set off with quotation marks. The Official Statement states in more than one place that the land, buildings and equipment were to be purchased for approximately $3.9 million. The discrepancy between the price paid for CTI's assets and the "in continued use" appraisal is referred to "in the opinion of management . . . as unrecorded equity due to the favorable negotiated purchase price." App. 120. As the district court pointed out,

> The suggestion that the investors were falsely led to believe that the property "would be adequate to prevent loss" if the business failed is a thinly veiled assertion that investors interpreted the assets' "fair market value in continued use" to mean the amount of money that piecemeal forced disposition of the assets would bring upon failure of the business. No reasonable investor could interpret the defendants' representation in this manner. By its very terms, the value of assets "in continued use" is antithetical to the

> value of the assets upon disposition after failure of the business. It was thus implicit in the language used in the Official Statement that an appraisal of the value of the assets "in continued use" was measuring something different from the value of the assets upon liquidation of the business. The terms used in the Official Statement cannot reasonably be taken as a representation that investors would not lose their investment if the business failed.

Id. at 68-69.

The Official Statement also contained disclaimers and stated in bold type that the foregoing statements regarding "certain risks associated with the offering should not be considered as a complete description of all risks to be considered in the decision to purchase the bonds." *Id.* at 92. It warned investors that CTI's assets might not be free of creditors' claims, that CTI lacked working capital, that Justus Enterprises' new president was a "Turnaround Specialist," *id.* at 120, and that bondholders could suffer a loss "if the assets of the tenant and guarantor are insufficient to enable them to perform in full." *Id.* at 92. Taken together, these statements would lead reasonable investors to conclude that they risked losing their money if Justus Enterprises failed to turn the business around.

Plaintiff points to the district court's statement that the "orderly liquidation value" would likely be important information to a reasonable investor as demonstrating that the district court applied the wrong legal standard. Read in isolation, this might appear to be so. A reading of the entire opinion, however, reveals that the district court considered all of

plaintiff's evidence and discussed specific disclosures that communicated risks to bond purchasers, including that CTI was in a "troubled financial condition." *Id.* at 56. We agree with the district court that the omission of the "orderly liquidation value" appraisal did not render the Official Statement misleading.

B

Plaintiff next alleges that the omission of three assumptions upon which the "in continued use" appraisal was based rendered misleading the actual representations in the Official Statement; that the omission of these assumptions would lead investors to conclude that a liquidation of assets would protect against a loss.

The statements plaintiff asserts were improperly omitted from the Official Statement appear in American's September 1983 appraisal report and read as follows:

> Fair Market Value is defined as the estimated amount at which the property might be expected to exchange between a willing buyer and a willing seller, neither being under compulsion, each having reasonable knowledge of all relevant facts, with equity to both, and with buyer and seller contemplating the retention of the facilities at their present location for continuation of the current operations.
>
> . . . .
>
> We did not investigate any financial data pertaining to the present or prospective

> earning capacity of the operation in which the designated property is used. Our opinion of fair market value assumes that the prospective earnings will provide an [sic] fair return on the appraised value of the assets included in the appraisal, as well as assets not part of the appraisal, if any, and adequate net working capital.
>
> . . . .
>
> The appraised fair market value stated above is not intended to represent the amount that might be realized from disposition of the property in the open market for any alternate applicable use.

App. 81-83.

The first and third statements are similar in substance; they refine the meaning of the "fair market value in continued use." The Official Statement includes the "in continued use" qualifier and states that the bond proceeds are earmarked to purchase CTI's assets.[5] We agree with the district court that a reasonable investor would conclude the "in continued use" appraisal assumes a viable business operation and does not include a sale of those business assets for another purpose. We agree that disclosing these two assumptions is not necessary to prevent the Official Statement from being misleading.

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5. The Official Statement specifically encourages prospective investors to analyze "additional information in the form of the complete documents summarized herein." App. 92. Those documents were available by contacting Ranson & Co., Inc. whose address and telephone number appear in the Official Statement. *See id.*

Appendix A

Plaintiff asserts that the other omitted assumption, of a "fair return on the appraised value of the assets" and "adequate net working capital," should have been disclosed because they were lacking in CTI's operation which had not enjoyed financial success. However, bond purchasers were informed of the disparity between the purchase price and the "in continued use" appraisal, that the appraisal information was a summary of other available documents, and that Justus Enterprises sought to "turnaround" CTI's business operations. The message repeated throughout the Official Statement was that Justus Enterprises purchased an unprofitable business and that a variety of risks were inherent in the bond issue. CTI lacked adequate working capital and evidently did not generate a "fair return" because it was in a "troubled financial condition." App. 56.

The assumptions of a "fair return" and "adequate net working capital" are consistent with the concept of "fair market value in continued use" of CTI's assets. Plaintiff did not introduce evidence that the "in continued use" appraisal was inconsistent with standard accounting or appraisal practice, or that these assumptions were improper bases upon which to build such an appraisal. Reasonable investors might not agree on a precise definition of an "in continued use" appraisal, but the term logically precludes a business lacking adequate working capital and unable to provide a fair return. Investors were told about CTI's financial problems and the disparity in the purchase price. The reasonable investor would be placed on notice that the "in continued use" appraisal necessarily assumed adequate working capital and a fair return on the invested assets in an ongoing business.

Omitting the paragraphs complained of from the Official Statement did not "significantly alter[ ] the 'total mix' of

information made available." *Basic Inc. v. Levinson*, 485 U.S. 224, 231-32 (1988) (quoting *TSC Indus.*, 426 U.S. at 449). Thus, we agree with the district court that omitting these assumptions did not render misleading the appraisal information actually disclosed, and no reasonable jury could conclude otherwise.

AFFIRMED.

APPENDIX B — MEMORANDUM AND ORDER OF THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF KANSAS FILED JULY 21, 1994

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF KANSAS

JAMES H. CONNETT,

Plaintiff,

v.

JUSTUS ENTERPRISES OF KANSAS, INC., a/k/a JUSTUS CYLINDER TECHNOLOGY, INC., et al.,

Memorandum and Order

This matter is before the court on the plaintiff's Motion to Alter or Amend the Judgment and For New Trial. The positions of the parties with respect to the motion are clearly set forth in the briefs and the court finds that oral argument is unnecessary. *See* D.Kan. Rule 206(d). For the reasons expressed herein, the court finds that the motion should be denied.

The plaintiff in this case alleged that the defendants made certain misrepresentations and material omissions in connection with the sale of City of Chanute industrial revenue bonds. Two claims were alleged in the complaint, one under 15 U.S.C. § 78j(b) and SEC Rule 10b-5 and one under the Kansas common law of fraud. At the close of the plaintiff's case the court granted the defendants' motion for judgment as a matter of law under Rule 50 of the Federal Rules of Civil Procedure. Based upon the evidence presented, the court determined that no reasonable jury could find in the plaintiff's favor. In so

ruling, the court examined each of the misrepresentations and omissions alleged by the plaintiff and concluded that the evidence could not allow a jury to reasonably conclude that the defendants' representations were false or misleading.

In the motion now before the court the plaintiff challenges only one aspect of the court's ruling: the defendants' alleged omission concerning the appraised value of the project assets. The court will therefore limit its discussion to that issue. In sum, plaintiff contends that the court improperly drew factual inferences in the defendants' favor with regard to the appraisal and failed to recognize reasonable inferences from the evidence that a jury could draw in the plaintiffs favor.

The purpose of a motion to alter or amend the judgment is to allow the court to correct manifest errors of law. *See Committee for the First Amendment v. Campbell*, 962 F.2d 1517 (10th Cir. 1992). With that purpose in mind, the court turns to the plaintiff's allegations that the court improperly granted the defendants' motion. As an initial matter, the court notes that there no dispute as to the legal standard governing a motion for judgment as a matter of law. That standard is essentially the same as the standard governing summary judgment. The court may grant such a motion only if no genuine issue of material fact exists and must consider the evidence and all reasonable inferences therefrom in the light most favorable to the non-moving party. *Bacchus Indus., Inc. v. Arvin Indus., Inc.*, 939 F.2d 887, 893 (10th Cir. 1991).

Facts. The plaintiff contends that the defendants' representations in the Official Statement[1] concerning the

1. The court notes that the plaintiff's argument is based on the (Cont'd)

appraised value of the property that was to be acquired with the bond proceeds were false or misleading. The facts concerning the appraisal are for the mot part undisputed. In May of 1982, an appraisal of the assets of C.J.B. Industries, Inc. was performed by American Appraisal Company. The evidence indicated that American Appraisal is one of the largest and most respected appraisal companies in the United States. C.J.B. Industries had previously owned the assets being acquired in the Chanute Bond issue. American Appraisal was asked to determine the fair market value of the property as of May 31, 1982. The results of this appraisal were set forth in a written report. Exh. 8. The term "fair market value" was defined by the appraiser as "the estimated amount at which the property might be expected to exchange between a willing buyer and a willing seller, neither being under compulsion, each having reasonable knowledge of all relevant facts, with equity to both, and with buyer and seller contemplating the retention of the facilities at their present location for continuation of the current operations." The conclusion

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(Cont'd)

representations contained in the Official Statement. The court agrees with that approach. As the court noted in its Memorandum and Order of May 4, 1994, new issue announcements published by one or more of the defendants contained representations to the effect that the "total value of the property" to be acquired with the bond proceeds had been determined by an appraiser to be over $11 million. A more detailed representation concerning the appraisal was made in the Official Statement. Under these circumstances the court concludes as a matter of law that a bond purchaser could not reasonably rely solely on the representations concerning the appraisal in the new issue announcements. Knowledge of the more detailed explanation contained in the Official Statement must be attributed to bond purchasers, even if they failed to read that document. *See Zobrist v. Coal-X, Inc.*, 708 F.2d 1511, 1518 (10th Cir. 1983). Thus, the issue now before the court must be examined in light of the representation that appeared in the Official Statement.

section of the twenty page appraisal report included the following statement:

> We did not investigate any financial data pertaining to the present or prospective earning capacity of the operation in which the designated property is utilized. Accordingly, based upon the premise outlined, and on the assumption that the prospective profits will provide a fair return on the appraised physical plant assets and adequate net working capital, it is our opinion that as of May 31, 1982, the Fair Market Value of the property appraised is reasonably represented in the amount of ELEVEN MILLION TWO HUNDRED SIXTY-TWO THOUSAND DOLLARS ($11,262,000), distributed as follows: . . .

Exh. 68 at 20. The conclusion section also stated that "[t]he appraised fair market value stated above is not intended to represent the amount that might be realized from disposition of the property in the open market for any alternate applicable use." *Id.* American Appraisal issued an updated appraisal on September 30, 1983, in Which it concluded that the appraised value of the assets had not changed since the 1982 appraisal.

The defendants obtained the permission of the American Appraisal Company to include a description of the appraisal in the Official Statement. Exhs. 190, 194. American Appraisal recommended that the report be referred to as follows: "The total value of certain property as determined by it 'fair market value in continued use' based on an appraisal as of May 31,

1982 by a nationally known independent appraisal company, was in excess of $11 million." Exh. 194. American Appraisal's permission was based upon the understanding that this would be the only reference in the Official Statement to the appraisal. *Id.*

The following paragraph appeared in the Official Statement under a heading entitled "Description of Project":

> Bond proceeds will be used to acquire approximately five acres of land, two connected multi-purpose buildings totaling 77,000 square feet, and machinery and equipment owned by Cylinder Technology, Inc. ("CTI") in Chanute, Kansas. The total appraised value of the acquired assets, including those not acquired out of bond proceeds, as determined by its "fair market value in continued use" based on an appraisal, as of May 31, 1982, by a nationally known independent appraisal company, was in excess of $11,000,000. The Tenant is expected to pay approximately $180,000 for additional assets of CTI and new machinery and equipment, and to pay $105,000 for organizational and acquisitional expenses from Tenant's own funds.

Exh. 215 at 5.

In addition to an appraisal of the "fair market value in continued use," the American Appraisal Company prepared a

report in May of 1982 expressing their opinion as to the "orderly liquidation value" of the property of C.J.B. Industries. "Orderly liquidation value" was defined as "the amount that might be realized from piecemeal disposition of the property, assuming a reasonable period of time in which to complete the transaction." *See* Exh. 131. The orderly liquidation value of the assets was determined to be $1,534,000. On August 23, 1983, American Appraisal Company issued an updated letter expressing its opinion that the orderly liquidation value of the property as of that date had not diminished from May of 1982. Although there was some dispute concerning whether the defendants were aware of this liquidation value and the update letter, the court assumes for purposes of this motion that the defendants were aware of it at the time they made representations concerning the appraisal of American Appraisal Company and that the defendants decided not to include that information in the Official Statement.

The plaintiff contends that the defendants' disclosure of the "fair market value in continued use" appraisal was misleading in light of the fact that American Appraisal had also determined that the liquidation value of the assets was $1.5 million. Plaintiff has heretofore not made explicit the manner in which he contends he was misled by the disclosure of the appraisal, but plaintiff's Memorandum in Support of the Motion to Alter or Amend suggests that because the amount of the bond issue was approximately $6 million, the disclosure of the $11 million figure "[led] bond purchasers to believe that in the event of failure of Justus Enterprises of Kansas, Inc. and of the default of the personal guarantor Walter Justus, the property acquired with the bond proceeds would be adequate to prevent loss." *Id.* at 4.[2]

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2. The court notes that the plaintiff has not cited any testimony from the record to support this allegation.

Appendix B

Discussion. As a starting point for addressing the plaintiff's argument, the court must note the complete lack of any evidence suggesting that the "fair market value in continued use" appraisal was not accurate at the time it was made. When Mr. Connett was asked whether he was aware of any facts indicating that the $11 million appraisal was not accurate, he said, "I question whether the value was that high," but he was unable to cite any evidence that the appraisal was inaccurate. Indeed, the record contains no such evidence. Nor was any evidence presented to suggest that the valuation of the assets on a "continued use" basis was an improper measurement of value under these circumstances. Furthermore, no evidence was presented to suggest that the appraisal was conducted in a manner contrary to generally accepted standards of appraisal or accounting. *Cf. Ferber v. Travelers Corp.*, 802 F.Supp. 698, 708 (D.Conn. 1992) (Valuation of property complied with generally accepted principles of accounting and was not actionable under Rule 10b-5.)

Given the evidence in the record, the court must reject the argument that the defendants' representations concerning the fair market value of the assets were misleading. The suggestion that the investors were falsely led to believe that the property "would be adequate to prevent loss" if the business failed is a thinly veiled assertion that investors interpreted the assets' "fair market value in continued use" to mean the amount of money that piecemeal forced disposition of the assets would bring upon failure of the business. No reasonable investor could interpret the defendants' representation in this manner. By its very terms, the value of assets "in continued use" is antithetical to the value of the assets upon disposition after failure of the business. It was

thus implicit in the language used in the Official Statement that an appraisal of the value of the assets "in continued use" was measuring something different from the value of the assets upon liquidation of the business. The terms used in the Official Statement cannot reasonably be taken as a representation that investors would not lose their investment if the business failed.

For the same reason, plaintiff's argument that it was misleading for the defendants to fail to disclose the assumptions and limitations of the appraisal is unpersuasive. The issue is not whether the defendants could have more fully explained the facts pertaining to the bond issue, including the all of the assumptions underlying the appraisal of the assets.[3] It is always possible (particularly with hindsight) to argue that some fact should have been more fully explained. The issue before the court, however, is whether the representations made by the defendants can reasonably be considered false or misleading. As the court noted in its Memorandum and Order of March 4, 1994, even if the assumptions underlying the appraisal were not set forth in the Official Statement, it was clear from the terms of the Official Statement that "fair market value in continued use" constituted a term of art. (Although

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3. The plaintiff asserts that the defendants' relationship to the bond purchasers was that of a fiduciary, *see Plaintiff's Memorandum In Support* at 9, and seems to suggests that the defendants owed the bond purchasers a heightened duty of care concerning disclosures of relevant information. *Id.* at 9-10. The court must reject any suggestion that the claims in this case were based in whole or in part upon a heightened duty of disclosure owed by a fiduciary. Such a special relationship was not pled in the complaint and was not preserved as an issue in the pretrial order. Nor was the plaintiff's claim based upon any statutory duty other than the one set forth in § 10(b). The only duty at issue is the one incumbent upon all persons engaging in the sale of a security: the duty to refrain from making false or misleading representations.

plaintiff contends that such a conclusion is not supported by competent evidence, it was in fact supported by the testimony of Mr. Connett, *see* Tr. 4/20/94 at 113, as well as by the terms of the Official Statement.) The usage of this term would have at least alerted any reasonable investor that the appraisal was a valuation of the assets on a specifically defined basis. That definition was readily available to any investor who wanted to know the basis of the appraisal. More importantly, for the reasons outlined above it is clear that a reasonable investor could not have concluded that this term represented the amount that would be obtained from liquidation of the assets in the event of failure of the business. A valuation of the assets "in continued use" clearly assumed the existence of a going business concern.

Plaintiff also argues that disclosure of the appraisal was misleading because the description of risks contained in the Official Statement did not inform investors "that the value of the property might not be sufficient to secure their investment." This argument also fails as a matter of law. As the court has discussed above, the disclosure of the appraisal did not constitute a representation that investors would be protected from loss if the business failed. Moreover, investors were specifically informed that "it is possible that the bondholders could suffer a loss of part of their investments if the assets of the tenant and the guarantor are insufficient to enable them to perform in full under the guaranty agreement and the city is unable to re-let the project at a rate which, when added to whatever contributions are made by the guarantor, is sufficient to pay maturing principal of and interest on the bonds as they become due." Exh. 215 at 4. Additionally, investors were informed that the risks listed in the Official Statement "should not be considered as complete description

of all risks to be considered in he decision to purchase the bonds." *Id.* Taken as a whole, the Official Statement cannot be said to have misled investors as to the risks associated with the venture.

Finally, the court takes note of the plaintiff's objections to certain references by the court in its May 4, 1994 Memorandum and Order concerning the testimony of Mr. Engstrom and Mr. Taylor. As the plaintiff recognizes in his brief, the court's observations about the opinion testimony of these witnesses did not enter into the conclusion of the court that the representations in the Official Statement could not reasonably be considered misleading. *Plaintiff's Memorandum In Support of Motion to Alter or Amend* at 7. The court recognizes that these witnesses have interests adverse to the plaintiff and that the issue of whether a representation in the Official Statement can be considered misleading must be judged from the point of view of a reasonable investor — not from the point of view of the underwriter of the bond issue. The testimony cited by the court was relevant to certain issues, however, including the allegation by the plaintiff that the defendants were grossly negligent or reckless in not discovering the allegedly false representations. Based on the evidence presented, including the fact that the defendants obtained the approval of American Appraisal Company to refer to their appraisal in the manner set forth in the Official Statement, the court had serious doubts about whether the record contained sufficient evidence concerning the defendants' state of mind to require submission of that issue to a jury. Because of the court's conclusion that the representations could not reasonably be considered misleading, however, it was unnecessary to decide the issue of scienter.

Appendix B

Conclusion. For the foregoing reasons, Plaintiff's Motion to Alter or Amend the Judgment and for a New Trial is hereby DENIED.

IT IS SO ORDERED. This 21 day of July, 1994, at Wichita, Ks.

s/ Wesley E. Brown
Wesley Brown, U.S. Senior
District Judge

APPENDIX C — MEMORANDUM AND ORDER OF THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF KANSAS FILED MAY 4, 1994

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF KANSAS

Civ. No. 87-1739-WEB

JAMES H. CONNETT, et al.,

Plaintiffs,

v.

JUSTUS ENTERPRISES OF KANSAS, INC., a/k/a JUSTUS CYLINDER TECHNOLOGY, INC.,et al.,

Defendants.

Memorandum and Order

The plaintiff in this case alleged that the defendants made several false or misleading representations in connection with the sale of City of Chanute Industrial Revenue Bonds. The case was certified as a class action with the named plaintiff, James H. Connett, representing a class consisting of all persons who purchased City of Chanute, Kansas, Industrial Revenue Bonds (Justus Enterprises of Kansas, Inc. — Tenant) in the initial public offering and sale of the bonds, excluding the defendants and excluding any persons who purchased their bonds on the secondary market subsequent to the initial public offering. The remaining defendants in the case are: Ranson & Co., Inc., J.O. Davidson & Associates, Inc., Mid-Continent Municipal Investments, Inc., and Dickinson & Co.

Appendix C

Two claims were alleged in the fourth amended complaint: the first claim alleged a violation of § 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 and the second claim alleged fraud under Kansas common law.

This matter came before the court for a jury trial beginning April 19, 1994. At the close of the plaintiff's case, the defendants moved for judgment in their favor under the provisions of Rule 50(a) of the Federal Rules of Civil Procedure. The court ruled orally from the bench that under the evidence presented the defendants were entitled to judgment as a matter of law on the claims against them and the court informed the parties of the fundamental reasons for that ruling. This written Memorandum and Order will supplement the court's ruling from the bench.

Motion for Judgment As a Matter of Law.

Rule 50(a) provides in part:

> (1) If during a trial by jury a party has been fully heard on an issue and there is no legally sufficient evidentiary basis for a reasonable jury to find for that party on that issue, the court may determine the issue against that party and may grant a motion for judgment as a matter of law against that party with respect to a claim or defense that cannot under the controlling law be maintained or defeated without a favorable finding on that issue.

When a motion under Rule 50(a) is raised, the court must determine whether there is evidence from which a reasonable jury could find in favor of the non-moving party. In making this

legal determination, the court must consider the evidence and all reasonable inferences therefrom in a light most favorable to the non-moving party. *See Bacchus Indus., Inc. v. Arvin Indus., Inc.*, 939 F.2d 887, 893 (10th Cir. 1991). Such a motion may not be granted unless the evidence "points all one way" and is susceptible of no reasonable inferences that would sustain the position of the non-moving party; however, a "scintilla of evidence is not sufficient to justify submitting a case to the jury." *See Adams-Arapahoe School Dist. No. 28-J v. GAF Corp.*, 959 F.2d 868, 874 (10th Cir. 1992).

The plaintiff presented testimony in this case from two bond purchasers: the representative of the class, James H. Connett, and Gordon Henke. Each of these witnesses testified concerning their purchase of the bonds. Each indicated that they were impressed by representations made concerning Walter Justus' assets and income and value of the property being acquired with the bond proceeds. The plaintiff also presented the live testimony of three individuals involved in the preparation of the bond issue.[1] The first of these witnesses, Michael Schotts, was in the employ of Walter Justus at the time of the bond issue. He testified concerning his dealings with Carlos Taylor of Ranson & Company. Schotts indicated that he provided information to Taylor concerning an appraisal performed by American Appraisal, as well as a letter certifying Justus' annual income to be in excess of $5 million. Schotts testified that so far as he knew all the information he provided to Taylor was truthful. The plaintiff also called as witnesses two agents of Ranson & Company: Carlos Taylor and Eric Engstrom. Carlos Taylor was the employee of Ranson who was responsible for Ranson's investigation and preparation of the offering documents. Eric

1. The plaintiff also presented brief excerpts from the depositions of two other witnesses, Richard Beuter and Robert Colin.

Appendix C

Engstrom, a member of the law firm of Fleeson, Gooing, Coulson & Kitch, acted as special counsel for the underwriters in investigating and preparing the offering documents. The testimony of these witnesses indicated that the representations which the plaintiff contends are false were, by and large, obtained by Ranson from Walter Justus. Taylor and Engstrom each testified that they had previously been involved in numerous bond offerings. Each of these witnesses was qualified by experience to express an opinion as to the appropriate standard of care to be followed by an underwriter in presenting an industrial revenue bond offering to the public. Each of these witnesses offered his opinion that Ranson's conduct and investigation in this case comported with the appropriate standard of care for an underwriter. Each indicated that in his opinion the information that was included as part of the offering documents was adequate and appropriate to advise purchasers of the bonds both of the material facts concerning the bond issue and the risks associated therewith. This testimony (which was provided by the plaintiff's own witnesses) that Ranson followed the appropriate standard of care in connection with the presentation of the bond offering was unequivocal and was not contradicted by any testimony presented on behalf of the plaintiff or by any of the documents introduced by the plaintiff relating to the bond issue.[2]

For the following reasons, the court concludes that the evidence presented by the plaintiff is not legally sufficient to

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2. This evidence refutes the allegation in the pretrial order that the defendants were grossly negligent or reckless in not discovering the allegedly false representations. Reckless behavior is conduct that is "an extreme departure from the standards of ordinary care, and which presents a danger . . . that is either known to the defendant or so obvious that the actor must have been aware of it." *Hackbart v. Homes*, 675 F.2d 1114, 1118 (10th Cir. 1982). As is noted above, the only evidence presented by the plaintiff on this issue was to the effect that the defendants' conduct comported with the standards of ordinary care required of an underwriter.

support the plaintiff's claims. The court will address individually the alleged misrepresentations and omissions recounted in the pretrial order and the evidence that was presented in support of them.

1. **Net Worth of $25 Million.** New issue announcements published by the defendants in connection with the bond issue indicated to prospective purchasers that Mr. Justus, the personal guarantor of the bonds, had a net worth of $25 million in 1983. Similarly, the Official Statement informed investors that Mr. Justus' unaudited financial statement was on file with the underwriters and was available upon request. This unaudited statement, which was compiled by Coopers and Lybrand based on information provided by Walter Justus and which was thereafter provided to the underwriters by Mr. Justus, represented Justus' net worth to be approximately $25 million in 1983 on an "estimated value basis." (Exhibit 71).

The plaintiff contends that the defendants' representations concerning Mr. Justus' net worth were false and that Justus actually had a net worth in 1983 of less than $10 million. After considering all of the evidence presented by the plaintiff on this issue, the court finds that no reasonable jury could find by a preponderance of the evidence that the representation made by the defendants was false or misleading.

The plaintiff simply has not produced any evidence showing that Walter Justus did not have a net worth of $25 million in 1983. In response to the defendants' assertion at the summary judgment stage of this case that there was no evidence to show that the $25 million figure was false, the plaintiff argued that Mr. Justus' statement of property filed in connection with his bankruptcy in 1986 revealed assets with a market value of only $8 million, although Justus had estimated the value of his assets in 1983 at

approximately $31 million. As the court indicated in its Memorandum and Order of April 12, 1994, this document is not sufficient to show that the defendants' representation was false. A significantly lower market value for the same property three years later — assuming that it was the same property — does not by itself show that the earlier valuation was false. It is common knowledge that the market value of assets can fluctuate significantly over time; this is particularly true as to assets consisting of real property. Absent some evidence indicating that the difference between the market value of Mr. Justus' assets in 1983 and 1986 was not attributable to the market itself, it would be speculation to assert that the difference alone proves that the 1983 figure was falsely overstated.

Nor does the plaintiff's argument concerning Mr. Justus' net worth on a "cost basis" and an "estimated value basis" demonstrate that the defendants' representation was false. Referring to the May 1983 Coopers and Lybrand compilation financial statement for Walter Justus, the plaintiff points out that that document represented Justus' net worth to be about $24.7 million on an "estimated value basis" but only $9.5 million on a "cost basis." Plaintiff suggests that this "cost basis" figure is enough to show that the defendants' representation was false. As an initial matter, the plaintiff has not pointed to any evidence in the record explaining the "cost basis" or "estimated value basis," or how those figures were determined in the first instance. Nor was any evidence presented concerning whether generally accepted accounting principles require presentation of a person's net worth to include a disclosure of the cost basis of the assets or what the significance of the cost basis would be to a reasonable investor. In order to address the plaintiff's argument, it must be assumed that the "cost basis" has some reference to the historical cost to Mr. Justus of acquiring and operating the assets he owned as of December 31, 1982, and that the "estimated value" refers to

the "market" value of the assets as of December 31, 1982. By definition, the market value of an asset at a date subsequent to its purchase can differ significantly from the cost at which the asset was acquired. The existence of a disparity between these two figures, without more, does not allow one reasonably to conclude that one or the other must have been falsely represented. Given the evidence presented on this issue, a jury could reach a conclusion that the $25 million net worth figure was false only by speculating that market conditions in 1983 would not have actually supported a valuation significantly above the cost basis of the assets. Such a conclusion would be just that — speculation — and would not be a reasonable inference arising from the evidence presented.

2. **Trust allegations.** The pretrial order sets forth several alleged misrepresentations or omissions made to purchasers concerning the Justus Trust. First, the plaintiff alleged that the defendants falsely represented that the Justus Trust was an asset of Walter Justus. When this issue was first raised on summary judgment, the court denied the defendant's motion on the basis that the language in the Official Statement could reasonably be interpreted as a representation that the Trust was an asset of Walter Justus. This view was perhaps the result of an abundance of caution by the court to insure that the plaintiff would have a chance at trial to adequately explain all of the circumstances surrounding the representations made by the defendants. After hearing all of the plaintiff's evidence, however, the court now concludes that there has been no showing that the defendants represented to the plaintiff that the trust itself was an asset of Walter Justus. The brief reference in the Official Statement to the Justus Trust cannot reasonably be considered such a representation. This view of the evidence is also supported by the testimony of Mr. Connett, who testified that he understood when he purchased the bonds that the assets of the Trust were not assets

of Walter Justus and would not be available to satisfy Mr. Justus' guaranty obligations. Taken as a whole, the evidence does not support the contention that the defendants falsely represented that the trust was an asset of Walter Justus or that a reasonable investor would have been misled to believe that was the case by the representations that were made.

The second allegation concerning the trust in the pretrial order was that the defendants falsely represented that Walter Justus received $900,000 per year from the Trust. Several of the "new issue announcements" published by the defendants and the "salient features document" (Exhibit 180) made such a representation. The plaintiff also alleged that the defendants misrepresented to prospective purchasers that Walter Justus had the right to receive cash income distributions from the trust, when in fact distributions of income from the trust were discretionary with the trustee. In addressing these issues for purposes of the defendants' motion, the court first takes note of the relevant stipulations contained in the pretrial order:

> G. In 1983, Walter Justus received income from the Walter Justus Trust in two different ways: First, pursuant to a Land Contract dated December 22, 1981, by and between Walter Justus and the Walter Justus Trust, Walter Justus sold and the Trust purchased the Crestwood West Apartments from Walter Justus. Pursuant to the terms of that contract, the Justus Trust was obligated to pay Walter Justus $900,000 per year for 16 years. Second, discretionary income distributions from the Trust.

Appendix C

H. In 1983, Walter Justus actually received total cash from the Trust in the amount of $1,341,000.00. That amount included the $900,000 payment for the sale of the Crestwood West Apartments and $441,000 in discretionary distributions.

I. In 1982, Walter Justus received total cash from the Trust in the amount of $1,172,928.00. That amount included the $900,000 payment for the sale of the Crestwood West Apartments and $272,928.00 in discretionary distributions.

J. The Trust actually distributed $441,129.24 in discretionary income distributions to Walter Justus in 1983.

K. The Trust actually distributed $494,019.00 in discretionary income distributions to Walter Justus in 1984.

L. The Trust actually distributed $1,681,511.00 in discretionary income distributions to Walter Justus in 1985.

M. The Trust actually distributed $1,277,540.00 in discretionary income distributions to Walter Justus in 1986.

* * *

W. Neither the Official Statement nor any other part of the Bond documents represented

that the Trust would be a guarantor of the Bonds.

The court initially believed that the plaintiff was contending that the defendants' representations were misleading because the $900,000 that Justus had a right to receive annually from the trust was not interest income but was instead income from the sale of real property to the trust. In light of the evidence presented by the plaintiff, however, it is not clear to the court how, if at all, the plaintiff contends he was misled concerning the trust. At any rate, there has been no evidence from which a reasonable jury could conclude that failure to disclose the particular character of the $900,000 payments was an omission of a material fact. There is no evidence that the character of these payments as income from the sale of property, as opposed to income on the trust assets, would likely be considered important by a reasonable investor. The important fact to a reasonable investor would be appear to be the fact that Mr. Justus had a right to receive the payments, not how the payments were characterized. Similarly, the plaintiff has not demonstrated that he was misled by the defendants' failure to inform him of the spendthrift nature of the trust or the fact that income distributions were discretionary with the trustee. In those documents in which the defendants made representations concerning the trust, prospective purchasers were informed that Mr. Justus received income from the trust of $900,000 annually.[3] It is undisputed that Mr. Justus in fact had a contractual right to receive annual payments from the Trust of approximately $900,000 in addition to whatever discretionary income distributions were made. Taken together, the evidence fails to

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3. The Coopers and Lybrand compilation financial statement, which included a note stating that Walter Justus "has the right to receive cash income distributions" from the trust, estimated the value of those distributions to be under $800,000 per year. Exh. 71 at 2 and 9.

establish a misrepresentation or omission of a material fact concerning the trust. In essence, the plaintiff claims that he was led to believe that Justus had a right to receive $900,000 annually from the Trust. The undisputed facts show that Justus in fact had such a right. The court concludes that insofar as the trust allegations are concerned, no reasonable jury could find in favor of the plaintiff.

3. **$5 Million Annual Income.** The Official Statement contained the following representations:

> Walter G. Justus represents that his annual income in 1983 will be in excess of $5,000,000. He anticipates in the foreseeable future that his income will be at least equal to or greater than the above. The unaudited financial statement of Mr. Justus is on file with the Underwriters and is available upon request.

(Exhibit 215 at A-2.). This statement appeared in the Official Statement after the defendants received a letter from Justus that included the representations mentioned above. (Exhibit 156.) The plaintiff contends that this representation is shown to be false or misleading by virtue of Walter Justus' personal tax returns, which disclose that Justus reported "total income" on his tax returns in 1981, 1982, and 1983 of approximately $234,000, $171,000, and $980,000, respectively.

At the time this issue was raised on summary judgment, the plaintiff did not dispute the defendants' allegation that Mr. Justus actually received "cash income" from various interests (referred to by the plaintiff as "gross receipts") in an amount in excess of $5 million in 1983. The plaintiff argued that summary judgment was

inappropriate, however, because the defendants' use of the term "income" could be considered misleading in light of all the evidence. Although there was no evidence that the defendants had ever represented that Mr. Justus had *taxable* income of $5 million, the court denied the defendants' motion for summary judgment based on a belief that a jury question might exist because of the ambiguous nature of the term "income." The court noted in its previous memorandum that the defendants' statement could be considered a representation to prospective purchasers that Mr. Justus annually had $5 million "that was at least potentially available to satisfy his obligations under the guaranty agreement." The court further indicated that Justus' tax returns could support an inference that Justus had significantly less than $5 million available to pay the bondholders in the event of a default. In so ruling, the court assumed that the plaintiff would present evidence at trial showing the amount and disposition of all of Mr. Justus' income during the relevant period. Quite frankly, the court assumed that testimony of Mr. Justus concerning his income would be presented and some evidence would be presented to the jury to indicate why the defendants use of the term would be misleading to a reasonable investor. No such evidence was presented.[4]

The burden was upon the plaintiff to prove by a preponderance of the evidence that the representation suggesting Justus had annual income of $5 million was false or misleading. The evidence presented by the plaintiff fails to meet this burden.

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4. It is not clear from the evidence presented by the plaintiff how he contends that he was misled by the representations. Mr. Connett initially testified on direct examination that he understood the representation concerning Mr. Justus' "annual income" to mean gross income. He later retracted his use of the term "gross" but nevertheless indicated that he understood the term "income" to mean the amount of money Walter Justus received before paying expenses.

Appendix C

Under the circumstances, it was incumbent upon the plaintiff to come forward with some evidence showing the actual receipt and disposition of funds by Mr. Justus. The plaintiff could have shown that the representation was misleading by demonstrating that, because of the nature of Mr. Justus' obligations, he in fact did not have $5 million at least potentially available to satisfy his obligations under the guaranty agreement. Such a showing is not made simply by pointing to the funds that were reported and taxed as "income" on Justus' personal tax returns. This is not a legally sufficient basis to show that the representation was false or misleading. The jury could only find that the representation was false or misleading by engaging in speculation concerning the actual disposition of funds received by Mr. Justus.

A. *Loss Causation*. The court also concludes that the evidence fails to establish a sufficient basis for a reasonable jury to conclude that the loss suffered by the plaintiff was caused by the alleged misrepresentations of Walter Justus annual income, the trust income, or his net worth. Specifically, the plaintiff has not presented evidence of "loss causation." In order to show that a loss was "caused" by a misrepresentation, it is generally not enough for a plaintiff in a securities case to show that he purchased a security in reliance upon the misrepresentation. He must also show that the misrepresentation "touches upon the reasons for the investment's decline in value." *TGB, Inc. v. Bendis*, 841 F.Supp. 1538, 1563 (D.Kan. 1993). This requirement recognizes that the seller of a security does not become an insurer of the success of an investment simply by virtue of the fact that the purchaser may have bought the security in reliance upon the belief that certain facts existed. *Id.* Stated otherwise, "[t]he plaintiff must prove not only that, had he known the truth, he would not have acted, but in addition that the untruth was in some reasonably direct, or proximate, way responsible for his loss." *Huddleston v. Herman & MacLean*, 640 F.2d 534, 549 (5th Cir.

1981). Ordinarily, this means that the plaintiff must show that the decline in the value of his investment was connected to and a result of the misrepresentations of the defendants and was not from some other cause or causes. *See McGonigle v. Combs*, 968 F.2d 810, 820 n.9 (9th Cir. 1992), *cert. dismissed sub nom., Casares v. Spendthrift Farm, Inc.*, 113 S.Ct. 399 (1992).

The Chanute Bonds had value because of two potential sources of funds to pay bondholders: Justus Enterprises and Walter Justus. Clearly, part of the decline in the value of the Chanute Bonds after the default by Justus Enterprises was due to the insolvency of Walter Justus in 1986 when he was called upon to perform on the guaranty agreement. The question here concerns whether the plaintiff has offered evidence from which a jury could reasonably conclude that Justus' insolvency was connected to or a result of the alleged misrepresentations as opposed to being the result of other factors. Although Justus' inability to pay the guaranty was necessarily a function of his annual income and the value of the assets he owned, the record contains only a skeletal view of Justus' financial condition in 1986 and the jury could only speculate as to why Justus became insolvent. Specifically, the record contains virtually no illumination of the cause of the debts that apparently far exceeded the value of Justus' assets in 1986. The documents filed by Justus in connection with his petition in bankruptcy, which are relied upon by the plaintiff to show Justus' assets in 1986, indicate that Justus had debts in 1986 of over $63 million. (Exhibit 328.) Absent some evidence explaining the financial condition of Justus and the circumstances underlying his insolvency when he was asked to perform under the guaranty agreement, the jury would have no factual basis upon which to make a determination of whether the loss suffered by the plaintiff was a result of the defendants' conduct or was instead a result of some other cause or

occurrence.[5] This was an essential element of the plaintiff's case. Because the plaintiff failed to produce evidence that would support this element, the defendants are entitled to judgment as a matter of law.

4. $11 Million Fair Market Value in Continuous Use Appraisal. New issue announcements published by one or more of the defendants represented that the "total value of the property" to be acquired with the bond proceeds had been appraised by an independent appraiser to be in excess of $11 million. The following more complete representation appeared in the Official Statement:

> Bond proceeds will be used to acquire approximately five acres of land, two connected multi-purpose buildings totaling 77,000 square feet, and machinery and equipment owned by Cylinder Technology, Inc. ("CTI") in Chanute, Kansas. The total appraised value of the acquired assets, including those not acquired out of bond proceeds, as determined by its "fair market value in continued use" based on an appraisal, as of May 31, 1982, by a nationally known

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5. Justus' guaranty to the bondholders constituted a promise to pay them in the event of a default. The defendants represented that Justus had sufficient assets to make good on that promise as of 1983. The defendants did not represent to bond purchasers, however, that Justus' financial condition would remain as it was in 1983, nor was it represented that in the future Justus would always be financially capable of making good on his promise to pay. That was a risk assumed by bond purchasers. As part of the plaintiff's burden of proving causation, the plaintiff was required to present some evidence showing that Justus' insolvency in 1986 was at least related to the alleged misrepresentations and was not the inevitable result of other factors.

> appraisal company, was in excess of $11,000,000.

Exhibit 215 at 5. It is undisputed that the American Appraisal Company had in fact made such an appraisal of the assets of C.J.B. Industries, Inc., the company which had previously owned the assets being acquired in the Chanute Bond issue, and had provided Ranson with an updated appraisal of the assets. The evidence indicated that American Appraisal is one of the largest and most respected appraisal companies in the United States. The defendant Ranson obtained approval from American Appraisal to include such a description of the appraisal in the Official Statement. Exhibits 190, 194. American Appraisal's approval was conditioned upon the understanding that this would be the only statement made in the Official Statement concerning the appraisal. *Id.*

The plaintiff contends that the defendants' representation of the appraisal was misleading because the defendants failed to disclose several allegedly material facts, including: the assumptions and limitations upon which the appraisal was based; the fact that American Appraisal had appraised the property to be acquired at approximately $1.5 million on an "orderly liquidation basis"; and the fact that the company from whom the assets were to be acquired had been unable to operate at a profit, had gone through a bankruptcy and was insolvent.

As a initial matter, it must be noted that the representation contained in the Official Statement concerning the "continuous use" appraisal was a true statement of fact. The only way in which the plaintiff could recover for this representation is by showing that it was *misleading* when considered in light of the material facts that were not disclosed. When the issue of the "continuous use" appraisal was raised on summary judgment, the court found

that a jury question could be raised as to whether the defendants' representation was misleading. After hearing all of the plaintiff's evidence, however, it is clear to the court as a matter of law that the evidence as a whole fails to show that the defendants' representation was misleading.

The failure of the defendants to disclose the limitations and assumptions upon which the appraisal were based is cited by the plaintiff as one reason why the appraisal disclosure was misleading. It is clear from the terms of the Official Statement, however, that the appraisal of the fair market value of the assets "in continued use" constituted a term of art and was an expression of the value of the assets on a specifically defined basis. The fact that the assumptions and limitations underlying that definition were not included with the description of the appraisal does not make the representation misleading. A valuation of the assets "in continued use" clearly assumes the existence of a going concern. At best, the plaintiff's evidence shows only that the defendants did not fully explain the basis of the appraisal in the Official Statement. That fact by itself does not make the representation misleading.

The defendants' failure to disclose the appraiser's conclusion as to the value of the assets on an "orderly liquidation basis" is also relied upon by the plaintiff as a material fact that could have made the "continued use" appraisal misleading. Upon review of all of the plaintiff's evidence, however, the court concludes that although the liquidation value of the assets acquired would likely be considered ***important*** by a reasonable investor, the failure of the defendants to disclose it did not make their representation concerning the "continued use" appraisal ***misleading***. It was implicit in the language used in the Official Statement that an appraisal of the value of the assets "in continued use" was measuring something different than the value

of the assets on an "orderly liquidation basis." The Official Statement would indicate to any reasonable investor that the appraisal was based on a particular type of valuation that was distinct from the amount of money the assets might bring in the event of a liquidation or forced sale. It would be unreasonable for any investor to maintain that he or she was misled into thinking that the value of the assets "in continued use" was the same as the value of the assets when the business was discontinued and the assets were disposed of on an "orderly liquidation basis." The disclosure of one type of appraisal is not misleading simply because there existed a different type of appraisal that was not disclosed. The disclosure that was made was correct and accurate in all respects.

A third omitted fact which the plaintiff believes made the disclosure of the "continued use" appraisal misleading was an alleged failure on the part of the defendants to disclose that the predecessor business of Justus Enterprises had been unable to function as a going concern. As the defendants have pointed out, however, the Official Statement did indicate that CTI (the immediate predecessor of Justus Enterprises) had been in financial difficulty. The Official Statement represented that there could be no assurance that the purchase of the assets would be totally free of the claims of creditors of CTI and the statement set forth two potential claims against CTI. It also cautioned investors that the matters referred to in the disclosures concerning the prior owner could have a material adverse effect on the financial condition of Justus Enterprises. Appendix A of the Official Statement indicated that the new business, Justus Enterprises, should acquire potential orders "that CTI could not deliver due to lack of working capital." The appendix also indicated that the owner of CTI would be involved in the new business, but that new management would be provided by Justus Enterprises, including the new president, Jack McBride, who "is known in the industry

as a 'Turnaround Specialist.' " Taking all of the disclosures and disclaimers in the Official Statement as a whole, it is now clear to the court that a reasonable investor would have at least been on notice of the troubled financial condition of CTI. The plaintiff's contention that the "continued use" appraisal was misleading because investors were not informed that CTI was not viable as a going concern is untenable.

Considering the plaintiff's evidence as a whole, the court concludes that there is no legally sufficient evidentiary basis for a reasonable jury to find for the plaintiff on this issue.

5. **Underwriters of the Bond Issue.** The plaintiff alleged that the defendants falsely represented that each of them were acting as underwriters for the bond issue. Plaintiff contends that in actuality only Ranson & Co. intended to assume liability as an underwriter. Assuming that this fact was misrepresented to bond purchasers, the court finds no evidence to indicate that there is a substantial likelihood that a reasonable investor would consider this fact important in deciding whether or not to purchase the bonds. As such, the plaintiff has failed to establish the materiality of the representation and cannot recover damages thereon.

Conclusion.

The court concludes after considering the evidence presented by the plaintiff as a whole that the there has been no showing that the defendants knowingly made false or misleading representations or omissions of material facts in connection with the sale of the bonds and no showing that the losses claimed by the plaintiff were the result of the defendants' conduct. Accordingly, the court concludes that the defendants are entitled to judgment as a matter of law on the plaintiff's claim under Rule 10b-5 and for common law fraud.

Appendix C

IT IS THEREFORE ORDERED that the defendants' Motion for Judgment as a Matter of Law is GRANTED.

This 4th day of May, 1994, at Wichita, Ks.

s/ Wesley E. Brown
Wesley E. Brown
United States Senior District Judge

APPENDIX D — RULE, CONSTITUTIONAL PROVISION AND STATUTE INVOLVED

FEDERAL RULE OF CIVIL PROCEDURE 50

Judgment as a Matter of Law in Actions Tried by Jury; Alternative Motion for New Trial: Conditional Rulings:

(a) **Judgment as a Matter of Law.** (1) If during a trial by jury a party has been fully heard on an issue and there is no legally sufficient evidentiary basis for a reasonable jury to find for that party on that issue, the court may determine the issue against that party and may grant a motion for summary judgment as a matter of law against that party with respect to a claim or defense that cannot under the controlling law be maintained or defeated without a favorable finding on that issue.

(2) Motions for judgment as a matter of law may be made at any time before submission of the case to the jury. Such a motion shall specify the judgment sought and the law and the facts on which the moving party is entitled to the judgment.

(b) **Renewal of Motion for Judgment After Trial; Alternative Motion for New Trial.** Whenever a motion for a judgment as a matter of law made at the close of all the evidence is denied or for any reason is not granted, the court is deemed to have submitted the action to the jury subject to a later determination of the legal questions

raised by the motion. Such a motion may be renewed by service and filed not later than 10 days after entry of judgment. A motion for a new trial under Rule 59 may be joined with a renewal of the motion for judgment as a matter of law, or a new trial may be requested in the alternative. If a verdict was returned, the court may, in disposing of the renewed motion, allow the judgment to stand or may reopen the judgment and either order a new trial or direct the entry of judgment as a matter of law. If no verdict was returned, the court may, in disposing of the renewed motion, direct the entry of judgment as a matter of law or may order a new trial.

(c) **Same: Conditional Rulings on Grant of Motion for Judgment as a Matter of Law.** (1) If the renewed motion for judgment as a matter of law is granted, the court shall also rule on the motion for new trial, if any, by determining whether it should be granted if the judgment is thereafter vacated or reversed, and shall specify the grounds for granting or denying the motion for the new trial. If the motion for a new trial is thus conditionally granted, the order thereon does not affect the finality of the judgment. In case the motion for new trial has been conditionally granted and the judgment is reversed on appeal, the new trial shall proceed unless the appellate

court has otherwise ordered. In case the motion for a new trial has been conditionally denied, the appellee on appeal may assert error in that denial; and if the judgment is reversed on appeal, subsequent proceedings shall be in accordance with the order of the appellate court.

(2) The party against whom judgment as a matter of law has been rendered may serve a motion for a new trial pursuant to Rule 59 not later than 10 days after the entry of the judgment.

(d) **Same: Denial of Motion for Judgment as a Matter of Law.** If the motion for judgment as a matter of law is denied, the party who prevailed on that motion may, as appellee, assert grounds entitling the party to a new trial in the event the appellate court concludes that the trial court erred in denying the motion for judgment. If the appellate court reverses the judgment, nothing in this rule precludes it from determining that the appellee is entitled to a new trial, or from directing the trial court to determine whether a new trial shall be granted.

Appendix D

UNITED STATES CONSTITUTION, AMENDMENT VII

Trial by jury in civil cases.

In Suits at common law, where the value in controversy shall exceed twenty dollars, the right of trial by jury shall be preserved, and no fact tried by a jury shall be otherwise re-examined in any Court of the United States, than according to the rules of the common law.

15 U.S.C. § 78j:

Manipulative and deceptive devices

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange—

(a) To effect a short sale, or to use or employ any stop-loss order in connection with the purchase or sale, of any security registered on a national securities exchange, in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

Appendix D

(b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

(June 6, 1934, ch. 404, Title I, § 10, 48 Stat. 891.)